



Early Journal Content on JSTOR, Free to Anyone in the World

This article is one of nearly 500,000 scholarly works digitized and made freely available to everyone in the world by JSTOR.

Known as the Early Journal Content, this set of works include research articles, news, letters, and other writings published in more than 200 of the oldest leading academic journals. The works date from the mid-seventeenth to the early twentieth centuries.

We encourage people to read and share the Early Journal Content openly and to tell others that this resource exists. People may post this content online or redistribute in any way for non-commercial purposes.

Read more about Early Journal Content at <http://about.jstor.org/participate-jstor/individuals/early-journal-content>.

JSTOR is a digital library of academic journals, books, and primary source objects. JSTOR helps people discover, use, and build upon a wide range of content through a powerful research and teaching platform, and preserves this content for future generations. JSTOR is part of ITHAKA, a not-for-profit organization that also includes Ithaka S+R and Portico. For more information about JSTOR, please contact support@jstor.org.

ADVANCE LETTER ON GENERAL BUSINESS CONDITIONS

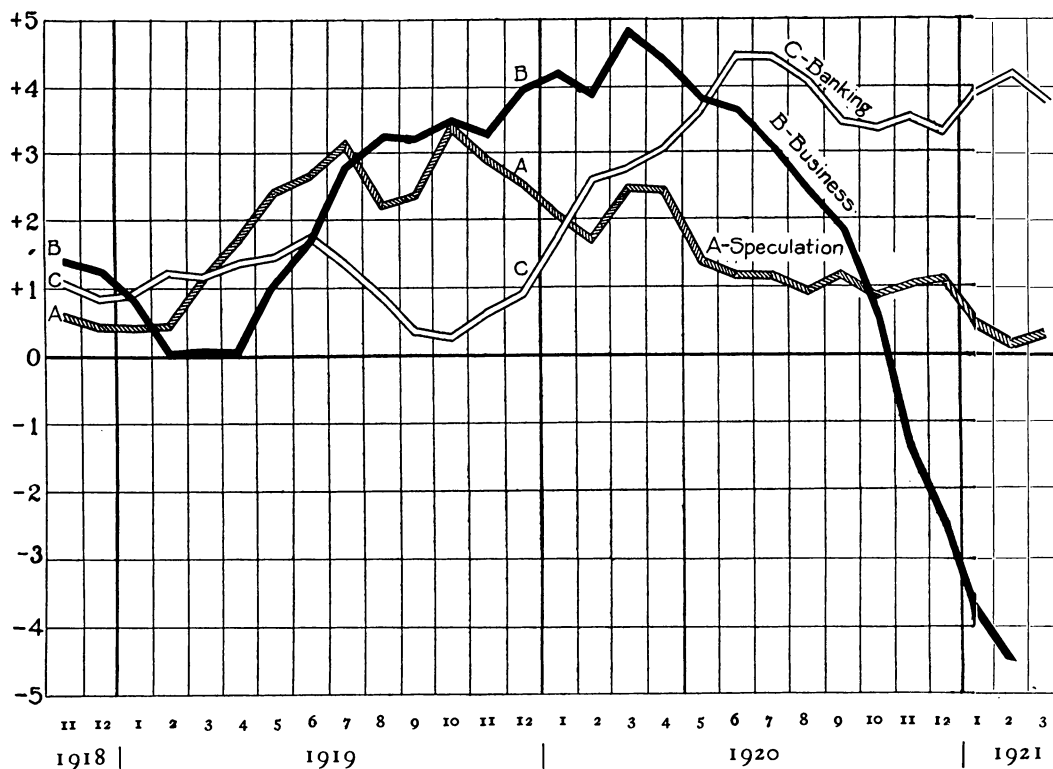
April 1, 1921

THE INDEX

THE movements of the curves of our Index Chart in March reveal no significant changes in the underlying situation. Curve C, rates on commercial paper (the importance of which we discussed in our last Letter), turned downward slightly; but it is not yet clear that this is the beginning of a persistent downward

16,680 millions, an increase of 15 per cent over the February figures, about the normal seasonal change.

The slump in stock prices in the middle of the month was followed shortly by a rally which carried industrials to their highest point for the year on March 23. During the last few days some of this gain has been lost, but prices are still generally above February quotations.



INDEX CHART. The items locating curves A, B, and C all refer to complete calendar months and the points are plotted in the middle of the spaces allotted to the months.

EXPLANATION: Each of the three curves on the Index Chart is obtained by averaging a group of statistical series, each group being composed of series homogeneous in character, i.e., when corrected for the seasonal influence and normal growth, the series of each group move in the same direction (upward or downward) at the same time. The series were all expressed in comparable units before averages were taken.

Our interpretation of the fluctuations of the three curves of the current index chart is based upon the relationship which was discovered among similar curves for the period 1903-14. All three curves had wave movements, but the upward swings and the crests of the waves were not reached simultaneously. The major movements of speculation preceded those of business by 4 to 10 months, and the movements of business preceded those of banking by 2 to 8 months. The sequence of movements holding for upward swings and crests also held for downward swings and troughs.

The persistent decline of curve A and the equally persistent rise of curve

C, both movements beginning in November 1919, indicated that a decline of business activity and commodity prices, curve B, would be inaugurated in the spring of 1920. In fact business unsettlement was noticeable in April and it has increased since that month while various indices of commodity prices have receded since May. The existence of the federal reserve system and the action of the banks in increasing rates and restricting credit made it appear very unlikely that the business readjustment indicated by the index chart would be accompanied by a financial panic. At this writing, we have passed the time in the business cycle when a financial panic would have occurred, if we were to have one.

Finally, the rise of curve C in January and February 1921 indicates that the period of readjustment of business will be prolonged at least until the summer of 1921. The prospect is a slowing down in the decline of wholesale commodity prices, a somewhat easier money market, and moderately higher security prices.

trend. The decline of curve C results partly from a slight fall in actual average rates and partly from the correction for seasonal variation; March rates in the past having ordinarily been above those of February.

Curve A, representing speculation, moved upward for the first time this year. This change, however, is entirely due to an increase in the number of shares traded last month; and since this increase is partly due to the greater number of trading days in March as compared with February, we attach little importance to this movement of the curve.

SPECULATION

The volume of sales on the New York Stock Exchange last month was approximately 16,090,000 shares, an increase of 58 per cent over the February total. In pre-war years March sales were about 20 per cent above those in February. New York bank clearings were

Probably the most important factor in this development was the marking down of call rates, which, though only fractional in most cases, was believed by some people to be a forerunner of easier conditions. Railroad stocks, having many unfavorable influences to contend with, were only slightly affected by the change in money rates.

Bond prices were also favorably affected by the fall of call rates, but not in anything like the same degree as stock prices, the rise from the low point of the month being less than a point in all classes except public utilities. In the case of bonds the influence of the money rate was apparently offset by the belief that further issues are contemplated.

BUSINESS

Changes in the general business situation are few, but these are favorable. The textile industries continue to

increase operations slowly, and buying in these lines, though still careful, is fairly encouraging. Recent figures issued by the Department of Commerce indicate that some 60 per cent of the spindles in the woolen and worsted mills of the country are now in operation, as compared with 45 per cent in January and 50 per cent in February. A similar improvement is reported by the shoe factories. The statistics of unemployment collected by the Department of Labor appear to indicate that, in general, conditions in this respect are on the mend. Car-loadings for the week ending March 5 were larger than for any previous week this year, the increase being noted in both grain and general merchandise.

In lines in which prices are still out of line with the general level there is continued stagnation, iron and steel being perhaps the most conspicuous. The signs of activity reported in the building trades are much less than one would expect at this season in a country complaining of a housing shortage; high building costs and high interest rates constitute an effective obstacle to new construction. Of course a certain supply of building materials can be disposed of eventually, even at present prices, but not enough to give employment to all the capital and labor now engaged in these industries.

BANKING

In attempting to derive a forecast of the money market from an analysis of the current banking situation one encounters great difficulties. The establishment of the federal reserve system makes pre-war banking movements of doubtful value as a standard of judgment. Furthermore, precedents that would enable us to draw conclusions as to the probable policy of handling the federal reserve system in times of business depression and revival do not exist. A "normal" federal reserve ratio has not been established. Whether the objective of the Federal Reserve Board is to maintain a ratio fluctuating between 50 and 70 per cent, 60 and 80 per cent, or some other standard can only be determined by experience. Another question of policy to be settled is whether the Federal Reserve Board will take the initiative in a depressed business situation and reduce the rediscount rates or wait until rates in the open market have dropped. Finally, at present the course of the domestic money market depends in large part upon developments in Europe.

Although there are many uncertainties in the present situation of the money market there are also some certainties. One certainly is this: the entire banking structure in the United States has been steadily growing stronger for the past four months. On March 25, 1921 total cash reserves of the federal reserve system reached the highest figure, 2,422 million dollars, in the history of the system. An increase of nearly one-fifth in cash reserves has taken place in the past year. In the same period (March 14, 1920 to March 25, 1921) the reserve ratio has risen from 42.2 per cent to over 50 per cent.

The peak of expansion of the banking system of the United States occurred last November. On November 5 the figure for paper discounted by the federal reserve

banks reached maximum, 2,827 million dollars; on March 25 the amount of paper discounted had fallen about 19 per cent. Federal reserve notes in actual circulation did not reach maximum (3,405 million dollars) until December 23, 1920 but the total outstanding on March 25 (2,931 million dollars) was 14 per cent below the maximum figure.

The improvement in the federal reserve banks to which we have referred is a result of improvement in the condition of member banks. Weekly reports of condition are not available for all member banks but only for about eight hundred "reporting banks." The reporting banks, however, have resources amounting to about two-thirds of all member banks and conclusions for member banks as a whole may safely be drawn from the reports of the eight hundred banks. On October 15, 1920 total loans and investments (exclusive of United States securities but inclusive of rediscounts with federal reserve banks) reached maximum, 15,854 million dollars; on March 18, total loans and investments had declined to 14,677 million dollars, or 7.4 per cent. On November 5, 1920 accommodation of member banks at the federal reserve banks reached peak, 2,278 million dollars; on March 18 the figures for borrowings had declined 559 million dollars or about one-fourth. In other words the reduction of 1,177 million dollars in loans and investments of member banks was paralleled by a reduction of 559 million dollars in borrowings from the federal reserve system.

The improvement in the banking situation which we have noted above has been general throughout the United States, although it has not been so great in the South as in other sections of the country. The reserve ratios of the various federal reserve banks, adjusted for inter-bank borrowing, indicate the widespread character of the improvement. On October 22, 1920 the adjusted reserve ratios of eight of the twelve federal reserve banks were below 38 per cent and five of the eight were below 25 per cent. On March 25, 1921 the adjusted ratios of all the federal reserve banks except Dallas were 42 per cent or over (Dallas having a ratio of 26.1 per cent). On October 22, 1920 inter-bank borrowings reached the maximum figure of 267 millions; on March 25, 1921 borrowings were reduced to 18 millions. On the whole, then, improvement in banking has been general, an encouraging feature of the situation.

During the past year wholesale prices have fallen about 40 per cent. In the face of a decline of 40 per cent in prices, a decline of 7.4 per cent in bank loans and investments does not look large. Further reduction appears to be inevitable. But it should be remembered that retail prices and wages (both factors in bank loans) have fallen much less than have wholesale prices. We may hazard the guess that even if there had been complete liquidation of bank loans they would not show a drop of more than 15 or 20 per cent. If we assume that prices become stabilized at approximately their present level, it seems probable that loans of the eight hundred banks will decline another billion. In any case, continued liquidation of bank loans appears to be a necessary condition for easier money rates.